MPAC Group plc

Upgrading forecasts after strong H1

16th July 2019

"*Don't fight the Fed*" is a tried and tested Wall Street strategy that has worked a treat over the past decade. Basically it states that when US interest rates fall, global equities should rise thanks to lower borrowing costs for consumers and corporates alike. Similarly after last week's dovish testimony to Congress by FOMC Chair, Jerome Powell, we believe this bias towards more monetary easing should keep the economy ticking along, and places a 'Put' under valuations.

Not that MPAC especially needs any outside help, given this morning's **positive H1 trading statement**. Indeed the **business is literally flying** with **FY19 results anticipated to be *"significantly above market expectations"*** - thanks to a rich seam of new orders for its advanced high speed production/packaging machines and complementary services. Underpinned too, by increasing demand for customerised 'end-to-end' & 'smart-enabled' solutions (re Industry 4.0).

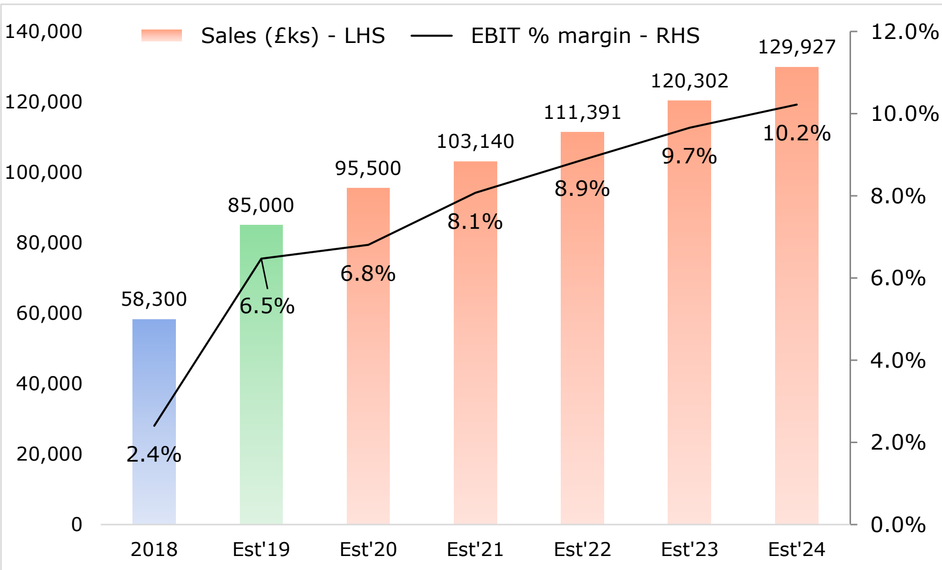
Greater demand coming from Healthcare

Better still, we suspect that a **big chunk of this incremental revenue is coming from the 'economically resilient' healthcare sector**, where a large contract was secured in 2018. Here there are multi-year upselling opportunities, involving upfront system design, factory equipment sales, implementation and ongoing service, spares & diagnostics

With regards to the numbers, we have **upgraded our FY19 & FY20 turnover forecasts to £85.0m** (+25% organic growth in packaging) & **£95.5m** respectively – which has likewise **pushed adjusted EBIT higher to £5.5m** (+20%, vs £4.6m before, £1.4m LY) and **£6.5m** (+2%, vs £6.4m) for this year and next.

Set for 25% FY19 LFL growth & improving margins

Increasing top and bottom line results



Source: Equity Development

Company Data

EPIC	**AIM:MPAC**
Price (last close)	155p
52 week Hi/Lo	220p/105p
Market cap	£31.3m
Net cash (Est. Dec '19)	£9.0m
Share count (incl Treasury)	20.172m
ED valuation/ share	260p
Avg. daily volume	25,000

Share Price, p

Source: Web Financial

Description

MPAC is a specialist provider of high speed production/packaging machines and complementary services with c. 510 staff. The group encompasses the design/manufacture of factory equipment and robotic solutions, as well as undertaking turnkey projects involving the design/integration such systems. >80% of revenues are generated outside of the UK, hence providing a natural hedge against further sterling weakness.

Core verticals are Pharmaceutical, Medical, Healthcare and Food/Beverage, supporting the likes of Nestlé, GSK, P&G, Philips, ConvaTec, AstraZeneca, Unilever, Kellogg's, Diageo, Ferrero, Hollister and CooperVision.

Next news: Interims 5th Sept '19

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£15m Lambert acquisition bedding down well

Elsewhere, **the integration of Lambert Automation** (purchased in May '19 for £15m) **is progressing to plan**. Not only generating economies of scale, but also supporting the group's key medical, healthcare and food/beverage verticals, alongside offering back office, property, supply chain, procurement and overhead savings, as the 2 firms are merged over the next 12-24 months.

Tony Steels adding: "***Trading is ahead of the Board's and market expectations, with the momentum gained in the latter months of 2018 continuing into H1'19****. The current order book, year to date order intake and the volume of quotation activity provides confidence in the prospects for the remainder of FY19.* ***The Board anticipates that profit for FY19 will be significantly above market expectations.***"

Excellent visibility for rest of FY19

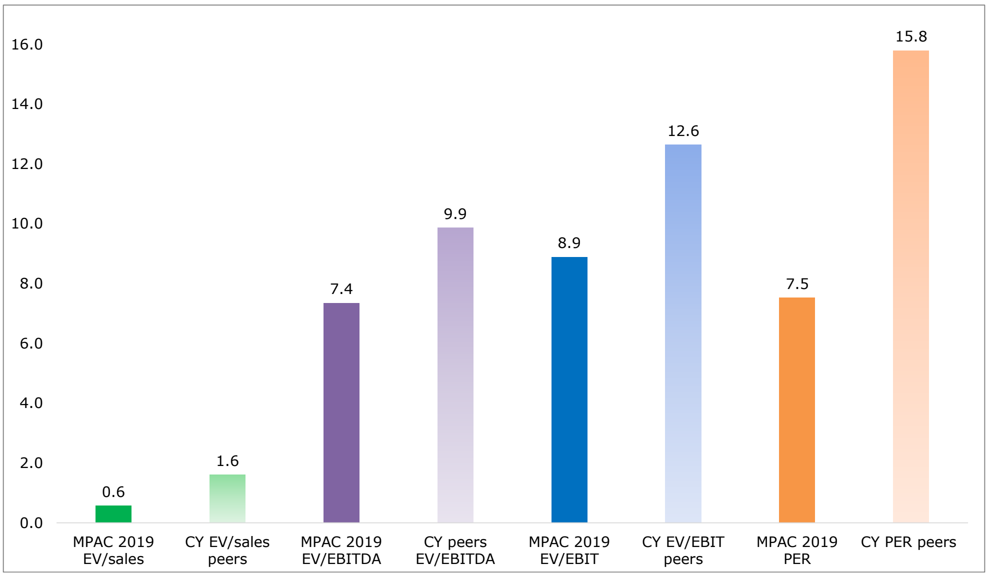
Moreover, last month the company said that the **actuarial deficit** relating to its **UK pension scheme had reduced from £69.9m in Jun'15 to £35.2m at Jun'18** – and importantly is now expected to be completely eliminated by Jul'24. 5 years earlier than previously envisaged.

Valuation lifted from 245p to 260p/share

Consequently, due to the strong H1 and encouraging outlook, **we have raised our valuation from 245p to 260p/share** – underpinned by **excellent visibility for H2'19**, based on YTD revenues, orderbook flow-through and normal repeat service business. Plus, with **>**80% of revenues generated overseas, there's also a natural hedge for UK investors against additional currency depreciation (£:$1.26 spot), say in the event of a 'no-deal' Brexit.

Lastly, it is worth noting that at 155p the stock trades at an unwarranted discount (see below) to its engineering/packaging peers.

MPAC 2019 valuation benchmarks vs peers (see appendix)



Source: Equity Development (MPAC metrics have been pension adjusted, except for PER)

Key risks

- As demonstrated in past recessions, capital equipment volumes are typically exposed to the cyclical nature of the global economy.
- The large size of the UK (£377.7m of liabilities) & US (£22.5m of liabilities) defined benefit pension schemes compared to MPAC's market capitalisation.
- Currency exposure, trade tariffs, raw material price increases (eg steel, aluminium) and competition.
- MPAC is smaller than its rivals/clients (eg German and Italian) and could see margins squeezed.
- Slower than expected growth, higher costs and/or lower cash generation.
- Industry suffers occasionally from lumpy orders, protracted customer purchasing decisions and irregular cashflows over the period end.
- Long term trend towards clients outsourcing production to 'low cost' contract manufacturers.
- Continued industry consolidation could impact pricing and margins.

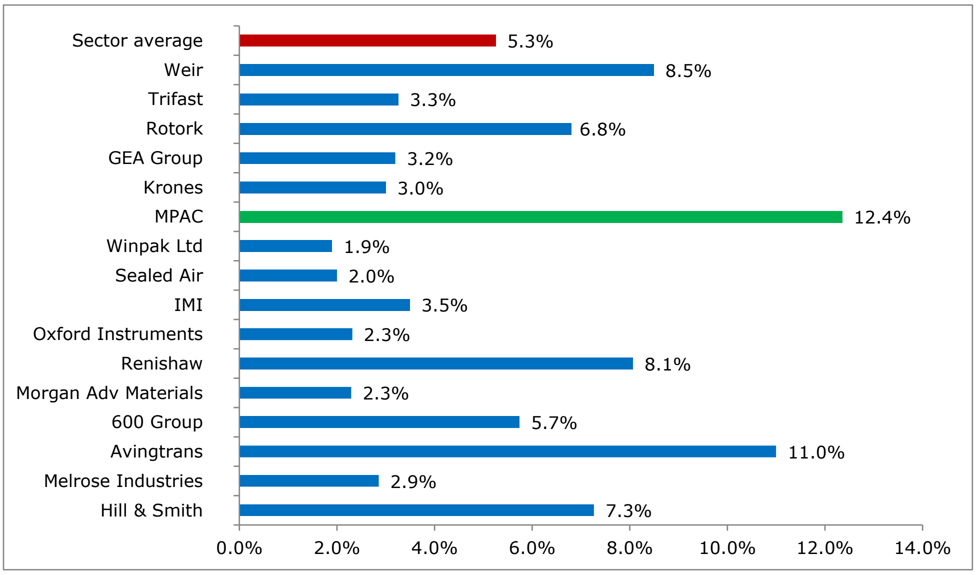
Adjusted financial projections

MPAC plc - continuing (December year end)	**2016 Act** £'000s	**2017 Act** £'000s	**2018 Act** £'000s	**2019 Est** £'000s	**2020 Est** £'000s	**2021 Est** £'000s	**2022 Est** £'000s	**2023 Est** £'000s	**2024 Est** £'000s	**2025 Est** £'000s
Closing orderbook	**25,500**	**34,400**	**39,800**							
Growth		*35%*	*16%*							
Equipment	28,800	40,400	46,200	57,750	58,000	62,640	67,651	73,063	78,908	85,221
Service	12,700	13,000	12,100	15,125	15,200	16,416	17,729	19,148	20,679	22,334
Lambert Automation				12,125	22,300	24,084	26,011	28,092	30,339	32,766
Turnover	**41,500**	**53,400**	**58,300**	**85,000**	**95,500**	**103,140**	**111,391**	**120,302**	**129,927**	**140,321**
Equipment		*40.3%*	*14.4%*	*25.0%*	*0.4%*	*8.0%*	*8.0%*	*8.0%*	*8.0%*	*8.0%*
Service		*2.4%*	*-6.9%*	*25.0%*	*0.5%*	*8.0%*	*8.0%*	*8.0%*	*8.0%*	*8.0%*
Lambert Automation					*83.9%*	*8.0%*	*8.0%*	*8.0%*	*8.0%*	*8.0%*
Total % YoY growth		***28.7%***	***9.2%***	***45.8%***	***12.4%***	***8.0%***	***8.0%***	***8.0%***	***8.0%***	***8.0%***
Equipment	5,400	9,200	9,300	11,719	11,832	13,154	14,545	16,074	17,478	19,004
Service	5,600	5,300	4,700	5,876	5,923	6,561	7,086	7,653	8,266	8,927
Lambert Automation				4,711	8,690	9,626	10,396	11,228	12,126	13,097
Total gross margin	**11,000**	**14,500**	**14,000**	**22,306**	**26,446**	**29,342**	**32,028**	**34,955**	**37,870**	**41,028**
Equipment	*18.8%*	*22.8%*	*20.1%*	*20.3%*	*20.4%*	*21.0%*	*21.5%*	*22.0%*	*22.2%*	*22.3%*
Service	*44.1%*	*40.8%*	*38.8%*	*38.9%*	*39.0%*	*40.0%*	*40.0%*	*40.0%*	*40.0%*	*40.0%*
Lambert Automation				*38.9%*	*39.0%*	*40.0%*	*40.0%*	*40.0%*	*40.0%*	*40.0%*
% Margin	***26.5%***	***27.2%***	***24.0%***	***26.2%***	***27.7%***	***28.4%***	***28.8%***	***29.1%***	***29.1%***	***29.2%***
EBITDA	**450**	**2,200**	**2,200**	**6,651**	**7,768**	**9,681**	**11,331**	**13,168**	**14,935**	**16,883**
% Margin	*1.1%*	*4.1%*	*3.8%*	*7.8%*	*8.1%*	*9.4%*	*10.2%*	*10.9%*	*11.5%*	*12.0%*
Distribution	-5,300	-5,400	-5,000	-7,050	-8,747	-9,306	-9,902	-10,536	-11,210	-11,928
Administration	-6,600	-7,300	-7,200	-9,264	-10,677	-11,165	-11,676	-12,209	-12,768	-13,351
Other	-300	-500	-400	-492	-522	-543	-565	-587	-611	-635
Adjusted EBIT	**-1,200**	**1,300**	**1,400**	**5,500**	**6,500**	**8,328**	**9,886**	**11,623**	**13,282**	**15,114**
% Operating Margin	*-2.9%*	*2.4%*	*2.4%*	*6.5%*	*6.8%*	*8.1%*	*8.9%*	*9.7%*	*10.2%*	*10.8%*
Underlying interest charge	-330	-170	0	0	0	0	0	0	0	0
Adjusted Profit before Tax	**-1,530**	**1,130**	**1,400**	**5,500**	**6,500**	**8,328**	**9,886**	**11,623**	**13,282**	**15,114**
Adjusted EPS (p)	**-6.0**	**4.2**	**4.5**	**20.6**	**24.2**	**31.0**	**36.6**	**43.2**	**49.4**	**56.2**
EPS growth rate			*7.8%*	*356.1%*	*17.6%*	*27.9%*	*18.1%*	*18.2%*	*14.3%*	*13.8%*
Dividend (pence)	***1.25***	***0.00***	***0.00***	***0.00***	***0.00***	***0.00***	***0.00***	***0.00***	***0.00***	***0.00***
Reported sharecount (Ks - incl Treasury)	20,172	20,172	20,172	20,172	20,172	20,172	20,172	20,172	20,172	20,172
Valuation benchmarks										
P/E ratio		*37.0*	*34.3*	*7.5*	*6.4*	*5.0*	*4.2*	*3.6*	*3.1*	*2.8*
PER (adjusted for pension recovery payments)					*19.9*	*12.8*	*9.9*	*7.8*	*6.5*	*3.1*
EV/Sales (pension adjusted)	*1.18*	*0.92*	*0.84*	*0.58*	*0.51*	*0.47*	*0.44*	*0.41*	*0.38*	*0.35*
EV/EBITDA (pension adjusted)		*22.2*	*22.2*	*7.4*	*6.3*	*5.1*	*4.3*	*3.7*	*3.3*	*2.9*
EV/EBIT (pension adjusted)		*37.6*	*34.9*	*8.9*	*7.5*	*5.9*	*4.9*	*4.2*	*3.7*	*3.2*
PEG ratio			*4.38*	*0.02*	*0.36*	*0.18*	*0.23*	*0.20*	*0.22*	*0.20*
Corporate tax rate	*20.0%*	*26.5%*	*35.7%*	*25.0%*	*25.0%*	*25.0%*	*25.0%*	*25.0%*	*25.0%*	*25.0%*
EBITDA drop through rate			*0.0%*	*16.7%*	*10.6%*	*25.0%*	*20.0%*	*20.6%*	*18.4%*	*18.7%*
Return on equity (%)		*1.9%*	*2.2%*	*9.2%*	*9.8%*	*11.2%*	*11.7%*	*12.1%*	*12.2%*	*12.2%*
Net cash/(debt)	**800**	**29,400**	**27,000**	**9,500**	**9,215**	**9,910**	**11,118**	**12,902**	**15,217**	**23,072**
Information only - Estimated non-underlying Pension charges										
UK pension recovery payments			-1,900	-1,940	-1,981	-2,022	-2,065	-2,108	-2,152	0
Topup UK pension payments above £5.5m EBIT			0	0	-330	-933	-1,447	-2,021	-2,568	0
UK pension admin costs			-900	-900	-918	-936	-955	-974	-994	-1,014
UK tax shield			532	540	613	739	849	970	1,086	193
US pension recovery payments (net tax shield)			-790	-751	-701	-651	-601	-551	-501	-451
Cashflow effect			**-3,058**	**-3,051**	**-3,316**	**-3,803**	**-4,219**	**-4,684**	**-5,129**	**-1,271**
Net cash/(debt) - pence per share		**146**	**134**	**47**	**46**	**49**	**55**	**64**	**75**	**114**
Net assets / diluted share (p)	175	212	201	222	246	277	314	357	406	462
Shareprice (p)	**155**									

Source: Equity Development. MPAC's EV has been adjusted for pension. The cost of UK PPF levy is included within EBIT.

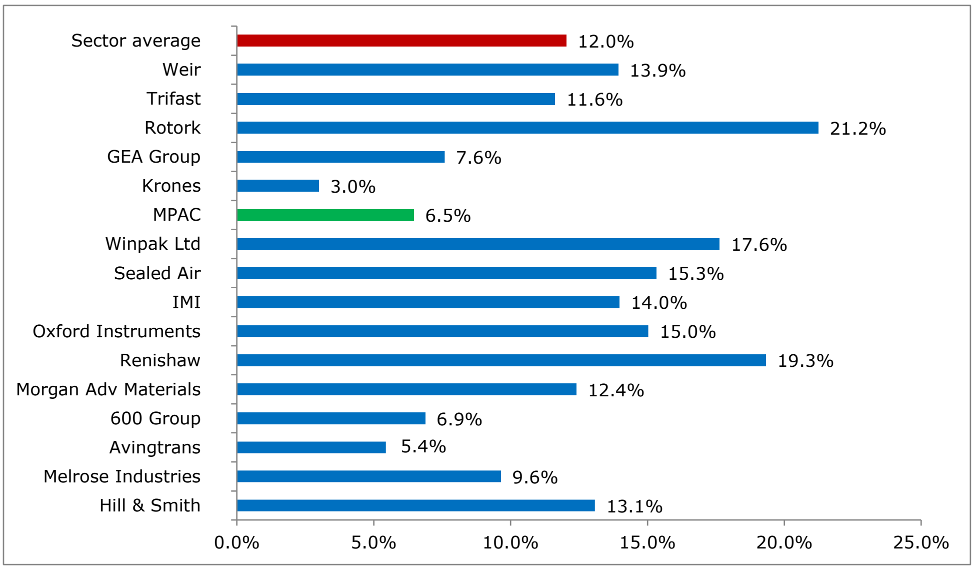
Appendix - Valuation benchmarks & industry KPIs

Current year + 1, sales growth rates



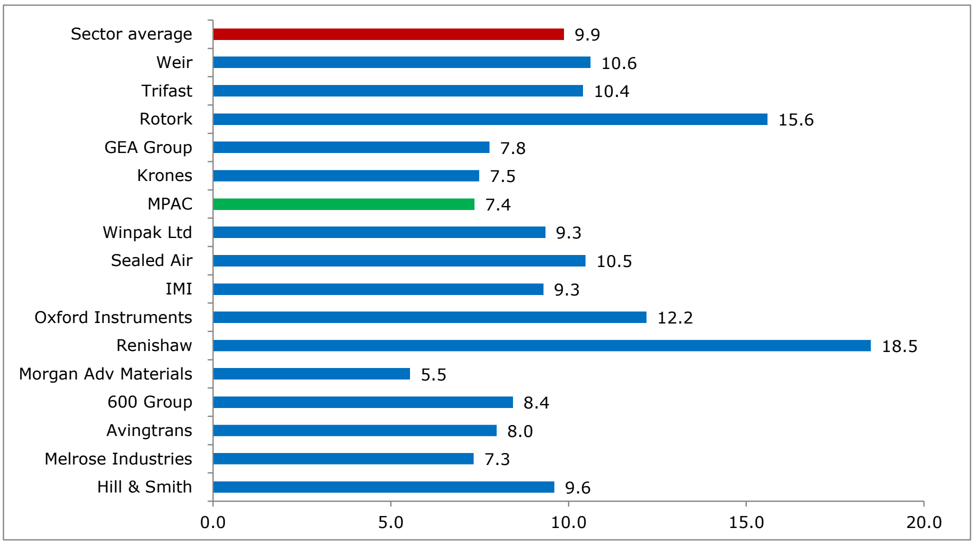
Source: Equity Development

Current year EBIT margins



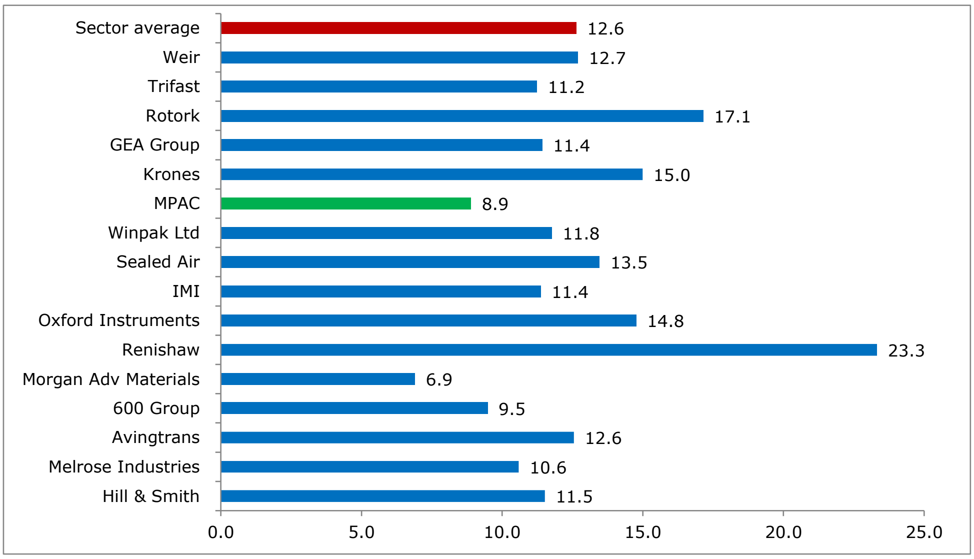
Source: Equity Development

Current year EV/EBITDA



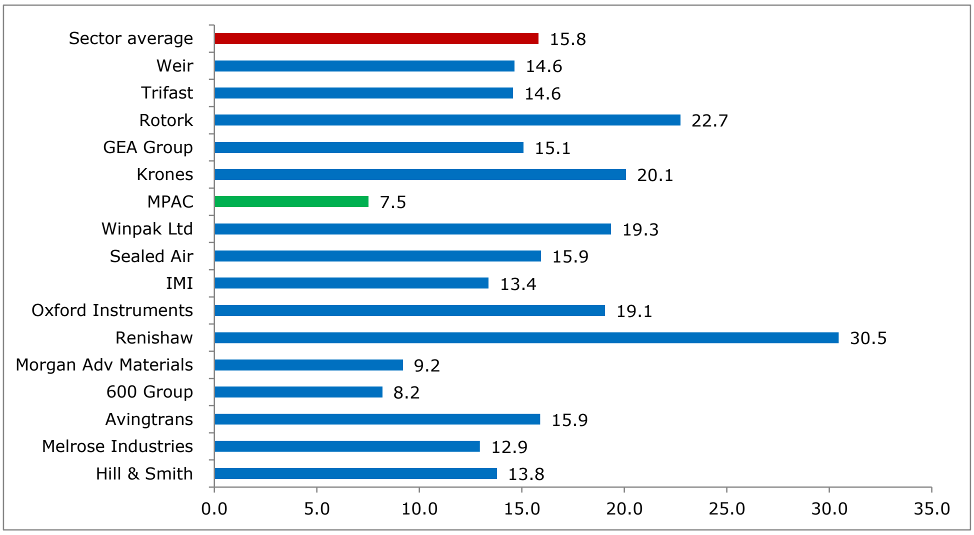
Source: Equity Development. MPAC pension adjusted

Current year EV/EBIT



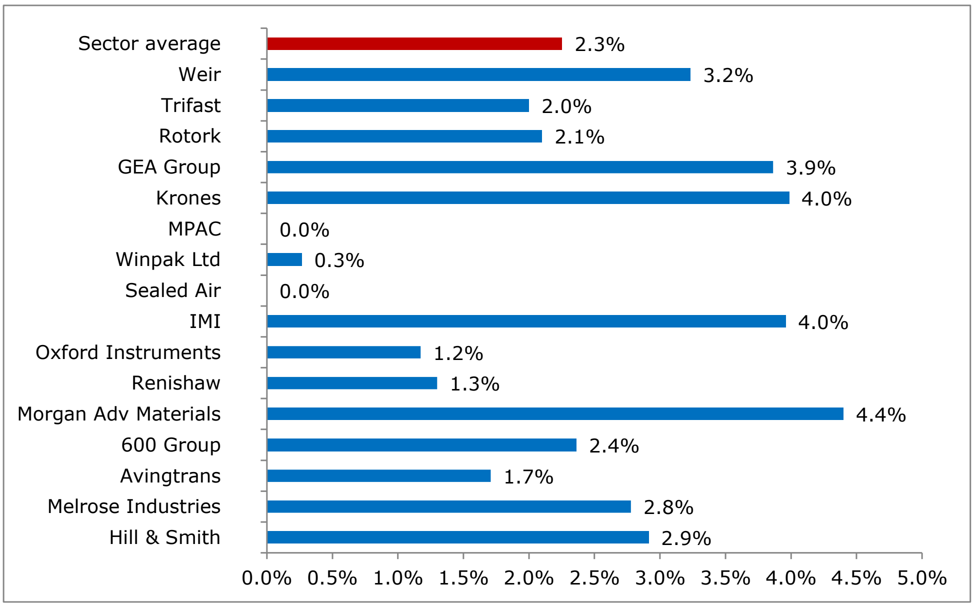
Source: Equity Development. MPAC pension adjusted

Current year PER



Source: Equity Development.

Current year dividend yield



Source: Equity Development

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